

[REDACTED]

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Mr Nicholas Rubin
Distribution Policy
Ofgem
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Dear Mr Rubin

Charges for pre-2005 Distributed Generators' use of Distribution Network Operators' (DNOs') distribution systems

Welsh Power is the owner of Leven, an OCGT that operates under STOR contracts with NGC as the SO. Leven, which was built in 1991, is connected into Central Networks and has always been a reserve provider.

Impact of Current Uncertainty

Leven as a pre-2005 generator currently pays no use of system charges, having paid for its connection in full at the time it was built. As it is connected at 11kV, before the announced boundary changes it would have been paid [REDACTED]/year under CDCM. Because of the boundary change, Leven will be classed as EHV and will be charged in the region of [REDACTED]/year.

The proposals put forward by Ofgem have therefore made the plant uneconomic and we will have to consider decommissioning it. This at a time when Ofgem says it is worried about peaking plant (Project Discovery) and the SO is calling for more reserve to be built to support intermittent generation and larger nuclear new build.

Ofgem talks about the charging regime needing to be altered to provide signals to generators. We are not sure what sort of signals Ofgem thinks that these sorts of changes in potential charges are sending. However, our experience is that it has created significant uncertainty and is undermining the economics of plant that have been built and operated on one basis for many years, adding to regulatory risk and jeopardising future investment.

Furthermore, as a company trying to invest in new plant connected to DNO networks, it has added uncertainty as to the type and location of connection investors may want to make. The different charging methodologies for EDCM further add to confusion and concern that Ofgem's recent interest in altering charges may see the methodologies moved to one agreed basis in future. This level of regulatory risk is making investment extremely difficult at a time when financing is already extremely trying.

Our Proposal

Welsh Power believes that Ofgem should allow Distribution Network Operators (DNOs) and their Distribution Connected Generators to remain bound by the terms of their connection agreements. While many of these are old, some are missing, etc, we believe that the intent of the agreements was very clear. The connection regime required the plant to pay upfront for the assets and work required to connect them. They then paid no charges, and received no payments, based on the understanding that they had already paid for the assets. When the assets reached the end of their lives the DNO would simply ask the generator to pay for their replacement.

Ofgem's proposals

The variability of the outputs from the different methodologies proposed in the consultation poses a significant commercial risk for generators as they will be unable to compete on a level playing field. We have no idea how a compensation mechanism could impact our plant and we have no desire to get into debates about how much compensation we should receive.

We remain concerned at the existence of two different methodologies (LRIC and FCP) for deriving EHV charges as both cannot be cost reflective when giving different charges to the same plant. This suggests to us that Ofgem will look to move all DNOs to one methodology in the longer term, which seems likely to mean plants face another price shock in some regions at a later date. Ofgem talks about discrimination, why is it not discriminatory to have one plant charged based on LRIC and another of FCP?

Costs vs Benefits

We would like to know what Ofgem believes the costs of negotiations with DNOs could be for smaller players in trying to sort out their compensation, then potentially appealing decisions (if there is anyone to appeal to). Not only will it take management time, but also lawyers will have to be drafted in and all of the changes explained to the bankers who finance such plants. The DNOs will also be racking up costs which will go back round to the customers as increasing Opex costs.

These costs do not have to arise if Ofgem leaves pre April 2005 distribution connected generators to simply go on not paying any direct charges until such time as their assets would normally be replaced. At that time, and not before, the generator would switch to being treated as any other connected party. Hopefully by then the basis for charging will have been standardised between DNOs and charges will be predictable and stable.

When do Generators Start to Pay?

The existing contractual arrangements should be allowed to go on for X years from the date of their connection, the value of X being set as follows:

1. If the existing agreement stipulates duration this should be used to define the term of the contractual right; or
2. If 1 does not apply (as the original contract does not exist) then X should be determined from the typical life of distribution network assets.

No generators should be allowed to move to the new regime, even if they would be paid under the revised charges. This will balance some winners against the losers and leave the overall charges relatively stable. In this way all generators would see the effect of DUoS charges around the period when they may be considering closure, thus having the desired economic affect at the time when it is important.

Impact Assessment

Regulators should ensure that the time and expenditure incurred in resolving a suspected defect or anomaly is proportionate. This is clearly not going to be the case in the proposals outlined by Ofgem's document. Given the potential impact (measured against the profits of some of these plants) we are surprised that Ofgem has not undertaken a cost benefit analysis of its proposals. Ofgem, DNOs and affected generators have already spent significant time, resource and finance on this issue, out of all proportion to the alleged, but unproven, benefit this new approach is aiming to deliver.

If Ofgem simply allows the grandfathering of rights that the these generators already thought they had, the costs of implementing the policy will fall significantly, even if implementation is spread over a number of years in the future. This seems to far better fulfil Ofgem's duties.

Should you have any questions please contact Lisa Waters on 020 8286 8677.

Yours sincerely



Alex Lambie
Chief Executive